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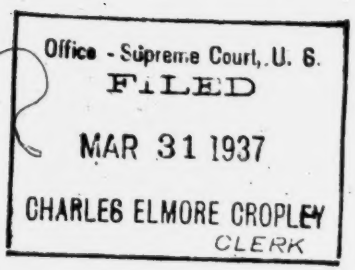

Supreme Court of the United States.

OCTOBER TERM, 1936.

No. [redacted] 19

BRADLEY W. PALMER, *Petitioner,*

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT AND BRIEF IN SUPPORT THEREOF.

ROBERT G. DODGE,
HAROLD S. DAVIS,
Attorneys for Petitioner.

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT.

To the Honorable the Chief Justice and Associate Justices of the Supreme Court of the United States:—

Bradley W. Palmer of Boston, Massachusetts, respectfully represents as follows:—

1. During the year 1929 the petitioner was the owner of common stock of The American Superpower Corporation (R. 69, 168).

2. On January 7, 1929, a corporation called The United Corporation was formed in fulfillment of a plan whereby certain securities then held by The American Superpower Corporation were to be exchanged for common and preferred stock of The United Corporation and whereby The American Superpower Corporation was to offer to its stockholders at $25 per share 821,472 shares of the 2,210,853 common shares of The United Corporation stock so received (R. 83-86, 170-171). The object of providing that

shares of The United Corporation stock should thus be sold to stockholders of The American Superpower Corporation was to build up the latter's cash position and to create a wide market for The United Corporation stock (R. 16, 167). For the purpose of the exchange the securities transferred by The American Superpower Corporation to The United Corporation were taken at agreed values substantially equivalent to the market value as of that time (R. 84-86). The Commissioner of Internal Revenue, for the purpose of fixing the tax liability of The American Superpower Corporation for 1929, later determined the aggregate value of the securities received by it to be the same as that of the securities transferred and of this total allocated a sum representing $25 per share to the common stock of The United Corporation (R. 89).

3. In accordance with the plan above described, the directors of The American Superpower Corporation on January 23, 1929, voted to offer to the common stockholders of record January 26, 1929, the privilege of purchasing at $25 per share one half of a share of the above-mentioned stock of The United Corporation for every share of common stock held in The American Superpower Corporation, this privilege to be evidenced by negotiable purchase certificates which should become void unless the privilege of purchase were exercised on or before February 15, 1929 (R. 16-17).

4. On May 1, 1929, and June 5, 1929, respectively, the directors of The American Superpower Corporation voted to give the common shareholders the privilege of purchasing additional stock of The United Corporation at $30 per share and stock of The Commonwealth & Southern Corporation (in the organization of which The American Superpower Corporation had participated in May, 1929) at $15 per share (R. 26-27, 33-35).

5. Pursuant to these votes the petitioner received on February 1, 1929, May 13, 1929, and June 23, 1929, respectively certificates giving him the privilege of purchasing 3,198 shares of The United Corporation at $25 per share, 1,599 shares of The United Corporation at $30 per share and 3,200 shares of The Commonwealth & Southern Corporation at $15 per share (R. 70, 72, 75).

6. On February 15, 1929, the petitioner exercised his option under the first set of purchase certificates and purchased the shares to which these referred, paying for such shares $79,950 (R. 168).

7. On May 24, 1929, the petitioner exercised his option under the second set of purchase certificates and purchased the shares to which these referred, paying for such shares $47,970 (R. 168).

8. On July 2, 1929, the petitioner exercised his option under the third set of purchase certificates and purchased the shares to which these referred, paying for such shares $48,000 (R. 168-169).

9. Each of these sales represented a considerable profit to The American Superpower Corporation over the cost of the property exchanged by it for stock of The United Corporation and of The Commonwealth & Southern Corporation respectively (R. 168-169).

10. The petitioner did not during the year 1929 sell or otherwise dispose of any of the stock purchased by him as aforesaid. Being advised that his receipt of the respective purchase certificates and the purchases made by him thereunder gave rise to no taxable income, he did not include in his return of income for 1929 any item reflecting these transactions (R. 169).

11. The Commissioner ruled in substance that the issue of these certificates constituted dividends and for this purpose were to be valued as of the dates upon which the rights to purchase stock of The United Corporation and of

The Commonwealth & Southern Corporation respectively attached to the stock of The American Superpower Corporation. The Commissioner placed a value on the first set of certificates of $12.50 per share of The American Superpower Corporation stock as of January 26, 1929, on the second set of $8.625 as of May 8, 1929, and on the third set of $.78⅛ as of June 18, 1929. The Commissioner accordingly held that the three issues of rights to the petitioner gave rise to total taxable income of $160,115.50 (R. 8, 61).

12. The Board of Tax Appeals upon the petitioner's application for a redetermination found as an inference from the facts set out in great detail in the stipulation filed by the parties (R. 68-161) that the purpose of offering the stock in question to the stockholders of The American Superpower Corporation was to build up its cash position and create a wide market for The United Corporation stock and not to distribute among the stockholders any of The American Superpower Corporation's earnings or assets (R. 167).

13. The Board further found from all the evidence that the fair market value of The United Corporation stock when offered by The American Superpower Corporation to its stockholders in January, 1929, was not more than $25 per share and held that the evidence did not disclose the fair market value of The United Corporation stock in May, 1929, or of The Commonwealth & Southern Corporation stock on the material dates (R. 170-171).

14. Upon these findings the Board came to the conclusion that the issue of the purchase certificates did not constitute a distribution by the corporation to its shareholders within the meaning of the governing statute,* that "the petitioner realized no taxable income from the re-

* Revenue Act of 1928, §115 (a).

ceipt of the purchase certificates involved in this proceeding or from the exercise of them in the purchase of shares of stock of United and Commonwealth" and that, "if and when he shall sell the shares acquired by him, the profit or loss must be predicated upon the basis of the price that he paid for them" (R. 176).

15. The Commissioner petitioned the Circuit Court of Appeals for the First Circuit to review the decision of the Board, the case being docketed in that court as No. 3100. The majority of the court after hearing rendered an opinion to the effect that "the rights themselves were [not] taxable income," but that "if exercised, the excess of value of the property acquired over the cash paid for it was a distribution of property and was taxable at its fair value" (R. 199). On the strength of the market quotations which were in evidence the majority further held that, notwithstanding the findings of the Board as to the actual value of the stock referred to in the purchase certificates, it had a value substantially in excess of the amounts paid for it and that "the excess value of . . . [the stock] above the price at which Superpower sold it was clearly a dividend," saying that the question was "not one of intention, but of what was in fact done" (R. 199). As to the dates with respect to which the value should be ascertained the majority said (R. 200):—

> "The value of the shares of stock should be determined as of the dates when the stock rights were exercised, viz.: under the first offering as of February 15, 1929, under the second offering as of May 24, 1929, and under the third one as of July 2, 1929, for these are the dates on which the taxpayer, in this case, in fact received taxable distributions. The dates taken by the Commissioner for this purpose were not the correct ones."

16. In a dissenting opinion Judge Wilson said (R. 202-204):—

> "This was not a distribution of corporate assets, but a sale at a price found by the Commissioner to represent the fair market value of the United stock. The cash received therefor by Superpower restored to it as assets the proportionate fair market value of the securities exchanged by Superpower for the stock of United.
>
> "We are not concerned with what might have resulted if the petitioner had sold the purchase certificates, or had sold the stock acquired after the exercise of his right to purchase. He did neither.
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> • • • • • • •
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> "There is no evidence that the offering of the stock of the United was intended by Superpower as a cloak for what in fact was a dividend. The Board of Tax Appeals found as a fact that it was not. This court cannot review this finding.
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> "Obviously the taxpayer cannot be taxed as income based on the selling price of the purchase certificates during the period he held them, since he did not realize income from them. If he failed to exercise them, he could claim no loss. *Eastern Shares Corporation* v. *Commissioner*, 32 B.T.A. 608. To him they simply represented a right to buy United stock. When exercised they became merely an acceptance of an offer to sell. If the stock proved to have an increased market value in the boom market of 1929 over the cash paid the company, he has not realized on it. To determine taxable income there must be a sale or exchange of property, or something definite other than a fluctuating

stock exchange market. The court does not recognize theoretical gains or losses."

17. In accordance with the opinion of the majority, the Circuit Court of Appeals on February 12, 1937, ordered that the decision of the Board of Tax Appeals be vacated and the case remanded to that Board for further proceedings not inconsistent with the opinion (R. 204). Upon the motion of the petitioner it was subsequently ordered that the issue of the mandate be stayed (R. 204).

18. The decision of the Circuit Court of Appeals presents the following points calling for review by this court:—

(*a*) As to what the result should be if it be assumed that the fair value of the stock purchased by the petitioner was more than the price paid by him to The American Superpower Corporation, the case involves issues upon which the decisions of the different federal tribunals are sharply in conflict.

(*i*) Since the question whether the transactions in question constituted sales or dividends is one of fact, the majority of the Circuit Court of Appeals, in assuming to hold that these transactions were dividends although the Board of Tax Appeals had found upon all the evidence that they constituted sales, acted in disregard of the well-settled rule that findings of fact by the Board are final. The case, therefore, presents the same necessity for intervention by this court as was deemed to exist in the very recent case of *Elmhurst Cemetery Association* v. *Commissioner*, 300 U.S. — (Feb. 1, 1937).

(*ii*) The Circuit Court of Appeals for the Second Circuit in *Ramapo, Inc.*, v. *Commissioner*, 84 F. (2d) 986, and the Circuit Court of Appeals for the Seventh

Circuit in *Commissioner* v. *Mayer*, 86 F. (2d) 593, have held upon states of fact similar to that now presented that the stockholder is taxable as for a dividend, though neither of these courts discussed the intention with which the sales were made or concurred except by inference with the ruling of the majority of the Circuit Court of Appeals for the First Circuit in the case at bar that this intention was immaterial. That ruling is, on the other hand, opposed to the decision of the Circuit Court of Appeals for the Fourth Circuit in *Helvering* v. *Bartlett*, 71 F. (2d) 598, and to that of the Circuit Court of Appeals for the Fifth Circuit in *Commissioner* v. *Cummings*, 77 F. (2d) 670, as well as to other decisions of the various Circuit Courts of Appeals with respect to analogous situations.

(*iii*) The conflict between the various decisions as to the dates as of which the value of the purchase certificates, if material, should be determined reflects fundamental differences of conception as to the nature of the transactions:—

According to the ruling of the Commissioner, it was the attaching of the rights to purchase stock of The United Corporation and of The Commonwealth & Southern Corporation respectively to the stock of The American Superpower Corporation that constituted the payment of dividends; on this view the value of the stock referred to in the purchase certificates should be ascertained with reference to the dates as of which the rights to purchase attached.

According to the ruling of the Circuit Court of Appeals for the Second Circuit in *Ramapo, Inc.*, v. *Commissioner*, 84 F. (2d) 986, it was the receipt of the purchase certificates by the stockholder that amounted to the receipt of a dividend; upon this assumption the amount

of the supposed dividends must be determined as of the dates when the respective certificates were received.

According to the view taken by the majority of the Circuit Court of Appeals for the First Circuit in the case at bar the issue of the certificates did not constitute the payment of a dividend, but the exercise of the rights evidenced by the certificates amounted to the receipt of a dividend; upon the respective dates when the rights were exercised the stockholder on this theory received taxable income in an amount equal to the difference between the amounts paid by him to The American Superpower Corporation for stock of The United Corporation or of The Commonwealth & Southern Corporation, as the case might be, and the values of such stock on those dates.

If the value of the rights is measured by the quotations in the market, the precise date as of which the value is determined is important, because the market quotations varied greatly from day to day.

(*b*) With respect to the value of the stock in question, the majority of the Circuit Court of Appeals likewise failed to follow the rule laid down by this court that findings of fact by the Board of Tax Appeals are final, assuming to disregard the findings made by the Board upon all the evidence and to draw their own inferences as to value from the facts set out in great detail in the stipulation. In this aspect, as in that referred to above, the decision in *Elmhurst Cemetery Association* v. *Commissioner,* 300 U.S. — (Feb. 1, 1937), is directly in point.

19. The questions presented are important not only to the parties, but to the public. The court will take notice of the frequency with which questions arise under the tax

laws as to whether a given transaction constitutes the payment of a dividend and of the fact that, as appears from the many cases both before the Board of Tax Appeals and before the courts involving transactions of this kind and from the lack of harmony in the several decisions, these questions are often of great difficulty. Definitive rulings are much needed for the guidance both of taxpayers and of the taxing authorities.

The petitioner therefore prays that a writ of certiorari issue out of this court to the United States Circuit Court of Appeals for the First Circuit commanding that the said case numbered 3100 be certified to this court for review and determination.

ROBERT G. DODGE,
HAROLD S. DAVIS,
Attorneys for Petitioner.

Supreme Court of the United States.

OCTOBER TERM, 1936.

No.

BRADLEY W. PALMER, *Petitioner,*

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

BRIEF FOR THE PETITIONER.

The present petition seeks the review of a decision (R. 204) rendered on February 12, 1937, by the United States Circuit Court of Appeals for the First Circuit whereby that court, upon the application of the Commissioner of Internal Revenue, reversed a decision of the Board of Tax Appeals in favor of the petitioner.

OPINIONS BELOW.

The opinion of the Board of Tax Appeals is reported in 32 B.T.A. 550; the opinions of the majority and minority of the Circuit Court of Appeals are not yet reported, but appear at pages 195 and 200 in the record respectively.

JURISDICTION.

The jurisdiction of this court to review the decision of the Circuit Court of Appeals is invoked under 28 U.S.C.

§347 (a) (Judicial Code, §240, as amended by the Act of February 13, 1925, c. 229, §1, 43 Stat. 938).

Questions Presented.

The petitioner received as a stockholder of The American Superpower Corporation certificates entitling him to buy of that corporation at specified prices shares of stock in other corporations owned by it. The petitioner availed himself of the opportunity afforded by the certificates and purchased the stock to which they related. The Board of Tax Appeals found as a fact (R. 170, 176) that the issue of the certificates and the purchase of stock by virtue of them was a *bona fide* sale and purchase and was not intended to constitute and did not constitute a dividend within the meaning of the governing statute (Revenue Act of 1928, §115a)* which reads as follows:—

> "The term 'dividend' when used in this title . . . means any distribution made by a corporation to its shareholders, whether in money or in other property, out of its earnings or profits accumulated after February 28, 1913."

The Board further found as a fact that the fair market value of the stock in question did not exceed the amount paid by the petitioner for it (R. 170-171).

Briefly stated the questions now presented are,—

(1) Whether, if it be assumed that the value of the stock in question was in excess of the prices paid by the petitioner, it was competent for the Circuit Court of Appeals

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* It may be noted that this provision is repeated without change in each of the subsequent Revenue Acts, so that a decision in the present case will affect transactions governed by these several acts.

to override the finding of the Board as to the nature of the transaction and to rule that the receipt of the certificates and the purchase of stock by virtue of them constituted a dividend.

(2) Whether, if it be assumed that there was such an excess of value and that the transaction constituted a dividend, the excess is to be ascertained as of the date when the rights attached to stock of record of The American Superpower Corporation or as of the date when the purchase certificates were received by the petitioner or as of the date when the petitioner exercised his option to purchase.

(3) Whether it was competent for the Circuit Court of Appeals to override the finding of the Board as to the fair market value of the stock in question and to hold that the value was materially more than the prices paid by the petitioner.

Statement.

For a statement of the facts material for the present purpose the petitioner begs leave to refer to the petition for certiorari.

Specification of Errors.

The petitioner's objections to the decision of the Circuit Court of Appeals may be summarized as follows:—

1. The court erred in not accepting the finding of the Board of Tax Appeals as to the nature of the transactions in question and in assuming to find that these transactions constituted dividends and gave rise to tax liability as of the dates upon which the rights evidenced by the respective purchase certificates were exercised by the petitioner.

2. The court erred in not accepting the finding of the Board of Tax Appeals as to the value of the stock which

the petitioner bought and in assuming to make different findings on that subject.

Argument.

For a summary of the argument which follows, the petitioner begs leave to refer to subdivision 18 of the petition for certiorari (pp. 7-9, *supra*). The differences between the results which are arrived at in the present case according as one or the other of the conflicting theories is followed may, however, be indicated by applying these several theories to the respective issues of purchase certificates:—

1. According to the ruling of the Commissioner of Internal Revenue, the petitioner received taxable income on January 26, 1929, May 8, 1929, and June 18, 1929, respectively, to the aggregate amount of $160,115.50 (R. 71-77).

2. According to the view taken by the Circuit Court of Appeals for the Second Circuit in *Ramapo, Inc.*, v. *Commissioner*, 84 F. (2d) 986, the petitioner received taxable income on February 1, 1929, May 13, 1929, and June 24, 1929, respectively, to the aggregate amount of $199,091.25 (see tabulations of market prices for these dates, R. 71, 74, 76).

3. According to the majority of the Circuit Court of Appeals for the First Circuit the petitioner received taxable income on February 15, 1929, May 23, 1929, and July 2, 1929, respectively, to the aggregate amount of $179,055 (see same tabulations).

4. According to the dissenting opinion in the case at bar and according to the view expressed by the Circuit Court of Appeals for the Fourth Circuit in *Helvering* v. *Bartlett*, 71 F. (2d) 598, and by the Circuit Court of Appeals for the Fifth Circuit in *Commissioner* v. *Cummings*, 77 F. (2d) 670, the petitioner received no taxable income at all.

I.

The Transactions Constituted Sales and not Dividends.

If the price paid by the petitioner was no more than the fair market value of the stock, there can be no tax liability on any theory. Even if it were conclusively established, however, that the price was less than the fair market value, it would not follow that the transactions were taxable.

It may be assumed for the sake of argument that a transaction which is in form a sale by a corporation to its stockholders may under some circumstances constitute a dividend. This, however, is true only when the transaction is in substance a dividend and is given the form of a sale merely to disguise its true nature. The general rule is that a sale by a corporation to its stockholders, even if the price is much less than the fair value of the property, is not taxable as a dividend.

> *Taplin* v. *Commissioner* (C.C.A. 6) 41 F. (2d) 454.
> *Van Vorst* v. *Commissioner* (C.C.A. 9) 59 F. (2d) 677.

In the case last cited the court said (at p. 680):—

> "It is earnestly contended that the transaction denominated a sale was in fact a 'dividend' within the meaning of §201 (a) [of the Revenue Act of 1924, corresponding to §115 (a) of the Revenue Act of 1928] in that it was in effect a distribution made by the corporation to one of its shareholders in property out of its accumulated earnings. . . . If this contention is to be sustained, it must be based upon the proposition urged that, because the consideration was so inadequate and the purchaser was the principal stockholder, it should for these reasons alone be regarded as a taxable distribution.
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> "The contention that a transaction which is in form a sale may, nevertheless, constitute a distribution to a stockholder of corporate assets or earnings may be conceded. It does not follow, however, that every such sale should be regarded as a distribution. . . . In the absence of other showing, the mere fact that the purchaser is a stockholder of the vending corporation does not change the character of the transaction."

Whether a given transaction constitutes a sale or a dividend is a question of fact largely dependent upon intention and to be determined according to the evidence in the particular case, just as it is a question of fact whether, for example, a bonus received by an employee is a gift or additional compensation.

Salvage v. *Commissioner* (C.C.A. 2) 76 F. (2d) 112.
Bass v. *Hawley* (C.C.A. 5) 62 F. (2d) 721.
Fisher v. *Commissioner* (C.C.A. 2) 59 F. (2d) 192.
Durkee v. *Welch* (D.C. S.D. Cal.) 19 F. (2d) 339.
Becker Brothers Co. v. *United States* (C.C.A. 2) 7 F. (2d) 3.
United States v. *Philadelphia Knitting Mills Co.* (C.C.A. 3) 273 Fed. 657.

The following extract from the opinion in *Schumacher* v. *United States,* 74 Ct. Cl. 720, illustrates the controlling significance of intention in situations of this kind (italics supplied):—

> "The plaintiff suggests the use of the words 'compensate employees' and 'additional compensation,' in the secretary's letter, 'merely emphasizes that inartistic and unintentionally misleading language was em-

ployed to describe what was *intended* to be, and what actually were, gifts.' We do not agree with plaintiff that these expressions are inartistic, or that they are misleading. The words 'compensate employees,' 'additional compensation,' and 'bonus' have a precise and well-understood meaning, and in the absence of any fact or circumstances showing they were not used in their ordinary sense they must be accorded their usual signification. *It is significant of the intention of the parties that the word 'gift' nowhere appears in the entire transaction. When the payments are referred to, they are invariably designated as 'additional compensation,' 'compensate employees,' or 'bonus' indicating beyond question that the payments were not gifts or gratuities.*

* * * * * * *

"We hold, therefore, that the payment of $100,000 to the plaintiff on January 2, 1925, by the stockholders' committee was *intended* to be, and was, additional compensation for services rendered."

In the present instance the Board of Tax Appeals has found,—and the propriety of the finding has not been questioned,—that there was no intention to distribute to the stockholders of The American Superpower Corporation any of its earnings or assets, but that *the purpose was to build up its cash position and to create a wide market for the stock of The United Corporation* (R. 167, 170). The price at which the first lot of The United Corporation stock was offered to the stockholders of The American Superpower Corporation represented, as noted above, the precise amount fixed by the Commissioner as the fair market value of that stock. The price paid by the stockholders was likewise the exact price paid by The American Superpower Corporation for the stock of The United Corporation and

of The Commonwealth & Southern Corporation measured by the value of the securities given in exchange (R. 89-91). As pointed out in the petition for certiorari (pp. 1-2, *supra*) the sale of this stock to the stockholders of The American Superpower Corporation was a part of the plan pursuant to which it was acquired.

It is thus apparent that, as the Board said, "no valid argument can be made that Superpower intended to distribute to its stockholders any portion of its assets by selling 821,472 common shares of United to them at a fair market value" (R. 170). Upon each of the three sales, moreover, The American Superpower Corporation realized a large profit with reference to the cost of the securities given by it in exchange for those sold (R. 168-169). So far as appears, the course pursued was an eminently judicious means of attaining the objects which the officers of The American Superpower Corporation had in view; there is nothing to suggest that it would have been more prudent to have thrown these large blocks of stock on the market and to have taken the chances as to sums realized.

The majority of the Circuit Court of Appeals in the case at bar said (R. 199):—

> "The question is not one of intention, but of what was in fact done. The statute defines dividend. . . . It says nothing about intention. The transaction is to be judged by the effect of it."

It is apparent that this assertion was wrong unless it can be said that under the particular circumstances disclosed in the present case the intention of the parties was immaterial and that, notwithstanding their intention, the transactions constituted dividends as matter of law. As shown by the cases cited above, this cannot be said merely because the price may have been less than the actual value of the stock. The precise question is whether a transaction fully intended

to be a sale and nothing else nevertheless constitutes a dividend as matter of law if there is present the additional fact that the property sold was offered to all the stockholders *pro rata*. The majority of the Circuit Court of Appeals for the First Circuit answer this question in the affirmative. The Circuit Court of Appeals for the Second Circuit,—in *Ramapo, Inc.*, v. *Commissioner*, 84 F. (2d) 986,—and the Circuit Court of Appeals for the Seventh Circuit,—in *Commissioner* v. *Mayer*, 86 F. (2d) 593,—have held that sales like those now in question constitute dividends, though neither court has ruled except by implication that the intention of the parties is immaterial. The dissenting judge in the present case, the Circuit Court of Appeals for the Fourth Circuit,—in *Helvering* v. *Bartlett*, 71 F. (2d) 598,—and the Circuit Court of Appeals for the Fifth Circuit,—in *Commissioner* v. *Cummings*, 77 F. (2d) 670,—answer the question in the negative. In *Helvering* v. *Bartlett* the court said (at p. 600):—

> "It seems clear that one is not to be taxed as upon income merely because he acquires an option which he might sell for value. If he allows the option to expire without exercising it, he has, of course, received no income. If he sells his rights under the option, he is taxable on the amount received on the sale. If he exercises it by making a purchase, his income from the transaction is determined on the basis of the profit realized when he sells the property purchased.
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> "In *Miles* v. *Safe Deposit & Trust Co.*, 259 U.S. 247, it was held that, where a stockholder sold rights to subscribe to new stock in a corporation, the amount thus realized was taxable as income; but the court pointed out that, if he had decided to accept the new shares instead of selling the rights, there would have been no

profit and hence no taxable income. It is true that in that case, it was the stock of the same corporation which was referred to; but the same principle would hold as to the purchase of stock of another corporation. No profit is realized upon a purchase; and the mere according of a right to purchase is not to be treated as a dividend or distribution of assets, unless these are in fact involved and the right to purchase is a mere cloak for a transaction which is essentially something else.

* * * * * * *

"Even a purchase at a bargain does not result in taxable income, unless used as a cloak for what is in fact a dividend. *Commissioner* v. *Van Vorst,* 59 F. (2d) 677.

* * * * * * *

"As has been often said, taxation is a practical matter. The income tax law is concerned, generally speaking, only with realized gains or losses. *Lucas* v. *American Code Co.,* 280 U.S. 445, 449; *Burnet* v. *Logan,* 283 U.S. 404, 413. And no gain has been realized by this taxpayer as a result of the allotment to him of the rights in question or of his purchase under those rights. That he might have realized a profit if he had sold the rights is beside the point. Taxes must be imposed on the basis of what has happened, not on the basis of what might have happened. It is important to note that the exact case here presented is covered by G. C. M. 7246, C. B. 1929, p. 80; and the administrative practice thus prescribed is entitled to great weight in determining the applicability of the statute which the government invokes. *Logan* v. *Davis,* 233 U.S. 613, 627."

At the hearing in the Circuit Court of Appeals it was suggested by the Commissioner that *Helvering* v. *Bartlett* was

distinguishable on its facts. Brief analysis, however, is sufficient to show *Helvering* v. *Bartlett* is substantially identical with the case at bar, especially with reference to the options issued by The American Superpower Corporation in January and June. In each of those instances the options were issued in connection with the original organization of the corporation whose shares were covered by the options. The only difference in point of fact is that in the Bartlett case, after the original corporation had voted to purchase 50,000 shares of the new company, it offered half of these shares to its shareholders at the same price and they were sold directly to the shareholders without the completion of the purchase by the original company. The original corporation had the right to buy the shares offered to its shareholders, would have had to take them up if they had not, and could have retained for itself, if it had so chosen, the excess value over the purchase price. It gave up this right to its shareholders; and the fact that the transaction did not go through its books furnishes no ground for distinguishing the case from the case at bar. This was in effect recognized in *Ramapo, Inc.,* v. *Commissioner,* 84 F. (2d) 986; the court made no attempt to distinguish *Helvering* v. *Bartlett,* but merely remarked that, "if *Helvering* v. *Bartlett* be deemed to hold the contrary, we cannot follow it."

In *Commissioner* v. *Cummings, supra,* which is likewise indistinguishable in principle from the case at bar, the court said (at p. 672):—

> "Taxation does not concern itself with hypotheses, but with real situations. *Helvering* v. *Bartlett,* 71 F. (2d) 598. The real situation here is that detachable stock rights, purchased and owned detached from the ownership of stock, and having a value of around $50 a right, were exercised. Had these warrants been sold, the gains would have been taxable as income. *Metcalf's*

Estate v. *Commissioner,* 32 F. (2d) 192; *Helvering* v. *Bartlett, supra.* They were not sold; they were exercised in the purchase of the stock. They were nothing but options to purchase stock. Neither their purchase nor their exercise resulted in taxable gain. They came into existence as property when they were purchased; they disappeared as property when, instead of being sold or exchanged as property, they were by their exercise merged into the executed contract represented by the stock they gave the right to buy. *Helvering* v. *Commissioner, supra.* The shares thus acquired came to the taxpayer as new property. *Wood* v. *Commissioner,* 75 F. (2d) 364. They may not be considered as standing for the options upon the exercise of which they were purchased, and therefore as held for more than two years prior to their exchange and sale. The result of the facts stipulated is that whatever the taxpayer might have done, what he did do was to exercise his rights to buy stock; that the exercise of this option gave rise to no taxable gain. It merely put him in the position of acquiring shares of stock as new capital, as to which, when he sold them, he had to account for the profits on the basis of their cost, which was the cost of the warrants, plus $30,050 cash paid when the stock was acquired."

The Board of Tax Appeals has consistently acted on the principle applied in the cases last cited.

Van Vorst v. *Commissioner,* 22 B.T.A. 632.
Everhart v. *Commissioner,* 26 B.T.A. 318.
Powel v. *Commissioner,* 27 B.T.A. 55.
W. M. Ritter Lumber Co, v. *Commissioner,* 30 B.T.A. 231, 274.
Freshman v. *Commissioner,* 33 B.T.A. 394, 403-404.

The petitioner submits that the view taken in these cases is clearly sound, but will not attempt at this time to elaborate this position. It is sufficient, the petitioner believes, to point out that the case at bar presents in this aspect a direct conflict between decisions of different Circuit Courts of Appeals with respect to a question whose general importance amply justifies examination by the court of last resort and that the decisions in the Second and Seventh Circuits cited above were made with very little examination of the controlling principles; in *Ramapo, Inc.*, v. *Commissioner*, 84 F. (2d) 986, it was, indeed, the taxpayer who contended that the issue of purchase warrants constituted a dividend.

The divergence of the decisions is further emphasized by the sharp differences of opinion noted above as to the date as of which the amount upon which the taxpayer is assessable should be ascertained, if it is assumed that the sales were equivalent to dividends. These differences result from the conflicting theories as to what it is that constitutes the dividend, if, indeed, there was any dividend at all. According to the decision in *Ramapo, Inc.*, v. *Commissioner*, 84 F. (2d) 986, it was the issue of the purchase certificates that amounted to the payment of a dividend; on this assumption the stockholder was taxable for the value of the stock to which the certificates referred even if he allowed the certificates to lapse and received no benefit from them at all. The majority in the case at bar, on the other hand, consider that it was the actual purchase which constituted the dividend and that, unless the stockholder either sold the certificate or exercised the privilege of purchase, he received no taxable income.

II.

The Finding of the Board of Tax Appeals as to the Value of the Stock in Question was conclusive.

Unless the fair market value of the stock when bought by the petitioner exceeded the prices paid by him, the transaction could not give rise to tax liability on any theory. The evidence before the Board of Tax Appeals consisted of a stipulation setting out a great variety of facts bearing on the question of value (R. 68-161). The Board was unable to find that there was in fact any excess of value and, indeed, made with respect to the first set of purchase certificates an affirmative finding that the value did not exceed the amount paid by the petitioner, *i.e.*, $25 per share (R. 170-171). Although the findings of the Board were in the nature of inferences drawn from the facts stipulated, these findings were no less binding on the Circuit Court of Appeals than they would have been if based on oral testimony.

Helvering v. *Rankin*, 295 U.S. 123.
General Utilities Co. v. *Helvering*, 296 U.S. 200.

It is true that the Circuit Court of Appeals was not concluded by the findings of the Board if these were wrong as matter of law. It is not, however, suggested that this was the case; on the contrary, it appears that the Commissioner, in determining the tax liability of The American Superpower Corporation for 1929, fixed the fair market value of the shares of The United Corporation held by it in January, 1929, at $25 per share (R. 89, 167). It was proper, of course, to consider daily quotations of the rights on the Curb, but these quotations were to be weighed with all the other evidence and were of themselves indecisive, espe-

cially when the abnormal conditions which existed in 1929 are considered.

San Francisco National Bank v. *Dodge*, 197 U.S. 70.
Strong v. *Rogers* (C.C.A. 3) 72 F. (2d) 455.
Heiner v. *Crosby* (C.C.A. 3) 24 F. (2d) 191.

The majority of the Circuit Court of Appeals in this respect fell into the same error as that corrected by this court in the very recent case of *Elmhurst Cemetery Association* v. *Commissioner*, 300 U.S. — (Feb. 1, 1937) and assumed to make findings *de novo* substantially as upon an appeal in equity. It is evident that this misconception obtains in the First Circuit no less than in the Sixth and that the intervention of this court is necessary if the functions of the Circuit Courts of Appeals in cases of this kind are not to be distorted.

The petitioner accordingly submits that his petition for certiorari is well grounded and should be granted.

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HAROLD S. DAVIS.